DEPARTMENT OF STATE REVENUE

04-20100111.LOF

Letter of Findings Number: 10-0111
Use Tax
For Tax Year 2007

NOTICE: Under IC § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Use Tax–Recreational Vehicle.

Authority: Gregory v. Helvering, 293 U.S. 465 (1935); Comm'r v. Transp. Trading & Terminal Corp., 176 F.2d 570 (2nd Cir. 1949); Horn v. Comm'r, 968 F.2d 1229 (D.C. Cir. 1992); Lee v. Comm'r, 155 F.2d 584 (2d Cir. 1998); IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-8.1-5-1; 45 IAC 2.2-3-4.

Taxpayer protests the imposition of use tax on the use of a recreational vehicle.

STATEMENT OF FACTS

Taxpayer is an individual and is a resident of Indiana. The Indiana Department of Revenue ("Department") determined that on January 28, 2007, Taxpayer purchased a recreational vehicle ("RV") in Kentucky and had been using the RV in Indiana without paying sales tax in any jurisdiction. As a result, the Department issued proposed assessments for use tax, ten percent negligence penalty, and interest. Taxpayer protests that the RV was titled by a Montana LLC, of which Taxpayer and his wife are the sole members, and that no Indiana sales or use tax is due. An administrative hearing was conducted and this Letter of Findings results. Further facts will be supplied as required.

I. Use Tax–Recreational Vehicle.

DISCUSSION

Taxpayer protests the imposition of use tax on the use and storage of an RV in Indiana. The Department imposed use tax after determining that Taxpayer had been using and storing the RV in Indiana and that no sales tax had been paid on the purchase of the RV. Taxpayer protests that the RV was titled by a Montana LLC and that all legal documents establishing the existence of the LLC were properly filed in Montana. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The sales tax is imposed by IC § 6-2.5-2-1, which states:

(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana.

(b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state.

The use tax is imposed under IC § 6-2.5-3-2(a), which states:

(a) An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

Also, 45 IAC 2.2-3-4 provides:

Tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used, or otherwise consumed in Indiana is subject to Indiana use tax for such property, unless the Indiana state gross retail tax has been collected at the point of purchase.

Therefore, when tangible personal property is acquired in a retail transaction and is stored, used, or consumed in Indiana, Indiana use tax is due if sales tax has not been paid at the point of purchase. The Department determined that Taxpayer purchased the RV in Kentucky in a retail transaction on January 28, 2007, and as a resident of Indiana, stored or used the RV in Indiana but did not pay sales tax anywhere. The Department therefore issued proposed assessments for use tax.

Taxpayer states that the Montana LLC's legal documents were properly filed by a Montana attorney. As explained in Taxpayer's January 26, 2010, protest letter, Taxpayer's reason for forming the LLC was that he and his wife felt that it was in their best interest that their traveling be covered under a limited liability company thus protecting them and their children with the hazards of travel.

As provided by Article III of the LLC's Articles of Organization (dated January 29, 2007):

The LLC is formed to conduct and promote any lawful business that acquires by purchase, lease, or other means any personal property and/or real property and to hold or dispose of it.

Also, the Articles of Organization establish that the LLC, the LLC's manager, and the LLC's organizer all share an identical address. In fact, the LLC's manager and the LLC's organizer are the same entity.

Article I, paragraph 3, of the LLC's Operating Agreement (dated January 31, 2007) states that:

The business of the LLC shall be the acquisition of real and personal property as the Members may agree

and to conduct or promote any lawful business within Montana or any other jurisdiction which a LLC is legally, allowed to conduct business.

Taxpayer also provided a copy of the minutes to the LLC's first and only meeting, at which the members agreed to execute any purchase agreements, notes or contracts as necessary for the purchase of the RV on behalf of the LLC. There is no mention of how the LLC would use the RV to conduct business but it is stated that the LLC, of which Taxpayer and his wife were the only members, would allow Taxpayer and his wife to operate the RV. The minutes of the meeting are dated January 31, 2007. Taxpayer also provided a copy of a letter from the Montana Secretary of State's office (dated January 30, 2007), which states that the Montana Secretary of State's office accepted the filing of the documents for the LLC.

These four documents, totaling seven pages of text, constitute the entire evidence of the LLC's existence. There are no documents establishing any business activity at all in Indiana, Montana, or any other state in the union. Plainly, the LLC was not pursuing its stated reason for existence, which was to conduct business. Neither do the four documents provide any explanation regarding how the formation of the LLC and the titling of the RV by the LLC would protect Taxpayer, his wife, and their children from the hazards of travel.

While the LLC made no attempt to undertake any business activity, the titling of the RV by the LLC did have a significant impact on Taxpayer's sales taxes. This leads to consideration of the "sham transaction" doctrine, which is long established both in state and federal tax jurisprudence dating back to Gregory v. Helvering, 293 U.S. 465 (1935). In that case, the Court held that in order to qualify for favorable tax treatment, a corporate reorganization must be motivated by the furtherance of a legitimate corporate business purpose. Id. at 469. A corporate business activity undertaken merely for the purpose of avoiding taxes was without substance and "[T]o hold otherwise would be to exalt artifice above reality and to deprive the statutory provision in question of all serious purpose." Id. at 470.

The courts have subsequently held that "in construing words of a tax statute which describe [any] commercial transactions [the court is] to understand them to refer to transactions entered upon for commercial or industrial purposes and not to include transactions entered upon for no other motive but to escape taxation." Comm'r v. Transp. Trading & Terminal Corp., 176 F.2d 570, 572 (2nd Cir. 1949), cert. denied, 338 U.S. 955 (1950). "[T]ransactions that are invalidated by the [sham transaction] doctrine are those motivated by nothing other than the taxpayer's desire to secure the attached tax benefit" but are devoid of any economic substance. Horn v. Comm'r, 968 F.2d 1229, 1236-7 (D.C. Cir. 1992). In determining whether a business transaction was an economic sham, two factors can be considered; "(1) did the transaction have a reasonable prospect, ex ante, for economic gain (profit), and (2) was the transaction undertaken for a business purpose other than the tax benefits?" Id. at 1237. The question of whether or not a transaction is a sham, for purposes of the doctrine, is primarily a factual one. Lee v. Comm'r, 155 F.2d 584, 586 (2d Cir. 1998).

In this case, the facts are that the officially stated purpose of the LLC's formation was to conduct business, but that the Montana LLC had no business functions and never attempted to conduct any business of any kind, and that the titling of the RV by the LLC did not provide any protection from the hazards of travel. The titling of the RV in Montana, a state without a sales tax, was merely an attempt to reduce or eliminate Taxpayer's sales and use tax liabilities. The formation of the LLC and the titling of the RV in the name of the LLC was therefore a "sham transaction."

Additionally, the RV was invoiced in Kentucky on January 28, 2007, while the LLC's documents were not signed or filed until January 29-31, 2007. This means that Taxpayer purchased the RV and then contributed it to the LLC. Since Taxpayer is an Indiana resident and he purchased the RV, he should have paid sales tax or use tax.

In conclusion, the formation of the LLC and the titling of the RV by the LLC was a sham transaction. Also, the timing of the purchase of the RV by Taxpayer and contribution of the RV to the LLC would still require sales or use tax be paid by Taxpayer. Either of these reasons alone would establish that Taxpayer acquired tangible personal property in a retail transaction, used and stored it in Indiana, but did not pay sales tax at the point of purchase or anywhere else. In such circumstances, Indiana use tax is due, as explained by 45 IAC 2.2-3-4.

FINDING

Taxpayer's protest is denied.

Posted: 05/26/2010 by Legislative Services Agency
An html version of this document.